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IN THE

Supreme Court of the United States

OCTOBER TERM, 1968

No. 635

IRVING D. FRIEDMAN and SYLVIA FRIEDMAN, on behalf of themselves and in a representative capacity on behalf of all other owners and/or holders of Baltimore and Ohio convertible 4½% income bonds due February 1st, 2010,

Petitioners,

—versus—

CHESAPEAKE AND OHIO RAILWAY COMPANY

and

BALTIMORE AND OHIO RAILROAD COMPANY,

Respondents.

BRIEF OF RESPONDENT THE BALTIMORE AND OHIO RAILROAD COMPANY IN OPPOSITION TO PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

EUGENE Z. DUBOSE
120 Broadway
New York, New York 10005
Attorney for Respondent The Baltimore and Ohio Railroad Company

JOHN L. ROGERS, JR.
RICHARD T. MCDERMOTT
Of Counsel

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Questions Presented

None of the nine questions sought to be raised by petitioners, with the possible exception of question 8 (Pet.* 6), is presented by the facts of this case. Most of these questions were not presented to the Courts below.

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* "Pet." refers to the Petition for a Writ of Certiorari.

This is a class action instituted by petitioners in the United States District Court for the Southern District of New York on behalf of themselves and other bondholders to recover interest and accelerated principal of a bond issue of respondent The Baltimore and Ohio Railroad Company ("B&O") due February 1, 2010. In the complaint petitioners allege that there was a "merger in fact" of respondent The Chesapeake and Ohio Railway Company ("C&O") and B&O with the result that C&O became a co-obligor on the bond issue. It is then alleged that C&O performed certain acts which, if performed by B&O, would have constituted a default under the terms of the Indenture securing the bond issue. The Indenture provides that no individual bondholder has a right to institute any action unless the Trustee (The Chase Manhattan Bank [N.A.]) refuses to sue upon written request of the holders of at least 25% in principal amount of the bonds with an offer of indemnity (generally termed a "no action" clause).

The District Court granted the motion of B&O for summary judgment dismissing the complaint upon the ground that, as a procedural matter, the "no action" clause of the Indenture barred the suit. At the same time the District Court denied petitioners' motion to amend their complaint to allege three additional alternative causes of action. This decision was affirmed by the Court of Appeals for the Second Circuit. Thus, the questions presented are:

1. Whether the "no action" clause in the Indenture is a bar to the prosecution of the instant action.

2. Whether the Courts below should have permitted petitioners to amend their complaint so as to set forth three proposed additional alternative causes of action which purport to allege violations of the Interstate Commerce Act.

Statement of the Case

Petitioners' complaint contains four causes of action. The first three causes of action are based on allegations to the effect that because C&O and B&O have consolidated certain operations, personnel and offices there was a "merger in fact" of the two railroads and thus that C&O became equally liable with B&O under the bond issue and the Indenture.

In their first cause of action petitioners allege that since C&O in February 1966 declared a cash dividend while there were arrears of interest on the B&O bonds, unpaid interest is now due and payable. This question is now moot since all of the back interest from 1961 through 1967 was paid on May 1, 1968 (4a; 395 F.2d at 664). The second cause of action, based upon the same allegations, alleges that the entire principal of the bond issue is now due and payable because of the alleged "default" arising from such payment of a cash dividend by C&O. The third cause of action alleges that there was a default under the Indenture resulting in the right to interest and accelerated principal because the "merged defendants" (C&O and B&O) failed to make sinking fund payments when C&O had paid dividends totaling $81,000,000 during the three-year period 1964-1966. The fourth cause of action alleges that there was a similar default accelerating principal and back interest because "B&O of the merged C&O-B&O" deposited certain amounts to fund B&O's retirement annuity plans. The papers submitted by petitioners in the District Court contained no facts supporting this last cause of action and there is nothing in the Indenture which would give any bondholder the right to make such a claim.

The answers of both C&O and B&O consist of general denials and two affirmative defenses. The second affirma-

tive defense in each answer is based on the "no action" clause of the Indenture which, as we have stated, bars individual bondholder suits unless the Trustee refuses to sue after written request by the holders of at least 25% in principal amount of the bonds together with an offer of indemnity.

B&O's motion for summary judgment was based upon the "no action" clause. It is conceded that the requirements of this clause have not been met. The District Court in granting summary judgment held that "[a]ssuming, *arguendo,* that the alleged events of default [as set forth in the complaint] have in fact occurred," the "no action" clause barred the suit (7a-8a; 261 F. Supp. at 730-731). In other words, the District Court held that regardless of the merits of their claims, and assuming that there had been defaults under the Indenture, petitioners had no standing to sue because of their failure to meet the conditions precedent to suit. In the District Court petitioners claimed that the "no action" clause did not bar the action since the Trustee had unreasonably refused to sue. With respect to this argument the District Court held that petitioners' contention that there was a "merger in fact" was without substance and that therefore the Trustee could not be said to have unreasonably refused to sue (10a-11a; 261 F. Supp. at 732).

The Court of Appeals affirmed the grant of summary judgment on the ground that the "no action" clause barred the action (3a; 395 F.2d at 664). It also stated that there was no issue of fact as to a merger since the ICC's approval of the use of joint facilities was not an approval of a merger as required by law under §5(2)(a)(4) of the Interstate Commerce Act (49 U.S.C. §5[2][a][4]) or the assumption by C&O of B&O's obligations as required by §20a(2) of that Act (49 U.S.C. §20a[2]).

Petitioners' "merger in fact" theory must be viewed against the background of the decision of the ICC granting C&O's application for stock control of B&O. In granting such application the ICC specifically held that "[b]efore C&O and B&O can effect such a merger, another application must be filed with this Commission." *Chesapeake & O. Ry. —Control—Baltimore & O. R.R.*, 317 I.C.C. 261, 265 (1962), the *Control Case*. As the District Court below stated, "railroads may not merge nor may one railroad assume the obligations of another without I.C.C. approval," citing §§5, 5(2)(a), 5(4), and 20a(2) of the Interstate Commerce Act (10a-11a; 261 F. Supp. at 732).

At the same time that B&O moved for summary judgment petitioners moved in the District Court for leave to amend their complaint to allege three proposed additional alternative causes of action.

The first of these sought to impose liability for principal and interest of the B&O bond issue upon the respondents and certain of their directors and officers under §20a(11) of the Interstate Commerce Act (49 U.S.C. §20a[11]). That section provides that any obligation assumed by a carrier where the authorization of the ICC is required shall be void if assumed without such authorization and that if any security evidencing such obligation is acquired by any person for value and in good faith without notice that the assumption is void, such person may bring an appropriate action for damages against the carrier, its directors, officers, etc. Petitioners did not allege that in reliance upon the alleged assumption of the bond obligations by C&O they acquired the bonds for value in good faith without notice that such assumption was void. The second and third proposed additional alternative causes of action sought to recover damages and reasonable counsel fees, respectively, for alleged violation of §8 of the

Interstate Commerce Act (49 U.S.C. §8). That section provides that a common carrier shall be liable for damages and reasonable counsel fees for any act performed by it which is prohibited or declared to be unlawful, or if the carrier shall omit to do any act required to be done, under the Interstate Commerce Act. Petitioners did not allege any facts showing that the damages they sought in the second alternative cause of action were causally related to any alleged violation of §8.

The District Judge after pointing out the fatal defects in these additional alternative causes of action held that the proposed amended complaint "alleges no facts showing that the damages sought are causally related to the alleged violations" (13a; 261 F. Supp. at 733-734). Furthermore, it held that it could not speculate what the ICC might do if it were asked to approve a *de jure* merger or assumption. Nor, it stated, could it guess what effect approval or disapproval would have on the payment of interest or principal on the bonds.

In affirming the District Court's denial of petitioners' motion to amend their complaint, the Court of Appeals for the Second Circuit adopted the reasoning of the District Court (4a; 395 F. 2d at 664).

Argument

Petitioners do not present any reasons for review of this case by this Court. They seek to raise various "constitutional" questions which simply do not exist. Furthermore, there is no merit to their arguments.

1. The first two contentions advanced by petitioners in their "Reasons For Granting The Writ" (Pet. 14-30) were not even remotely suggested by petitioners in the Courts below. These contentions are based on the assertion that

the decision of the ICC in aprcving stock control of B&O by C&O violated the due process, the equal protection and the contract clauses of the Constitution. Aside from the fact that these points were not raised below, petitioners' arguments intrinsically have no merit. The Interstate Commerce Act vests in the ICC the power to regulate and control the railroad industry. Under this power, which was clearly constitutionally granted to the ICC, that administrative body has the power to approve railroad mergers, to approve the acquisition by one carrier of stock control of another carrier, and to approve the assumption by one railroad of the obligations of another railroad. In this instance the ICC in 1962 approved stock control of B&O by C&O, specifically stating that "[b]efore C&O and B&O can effect * * * a merger, another application must be filed with this Commission." The *Control Case,* 317 I.C.C. at 265. The ICC has never approved any merger of the two railroads nor has it approved the assumption by C&O of B&O's debt obligations. Thus, to the extent that petitioners are objecting to the order of the ICC approving the acquisition by C&O of stock control of B&O, petitioners not only have failed to comply with the "no action" clause, but also have failed to follow the exclusive procedure for judicial review of orders of the ICC set forth in the Judicial Code (28 U.S.C. §§2321, 2322, 2323, 2324, 2325, 2284(1), (2) and 1253). See *Schwartz* v. *Bowman,* 244 F. Supp. 51, 66-68 (S.D.N.Y. 1965), *aff'd per curiam,* 360 F. 2d 211 (2d Cir. 1966), *cert. denied,* 385 U.S. 921 (1966).

Petitioners cite no case which holds that stock control by one railroad of another can result in a "merger in fact" of the two railroads and no such authority will be found. Petitioners point to the fact that B&O and C&O have combined certain offices, have filed consolidated tax returns, have published combined annual reports and consolidated financial statements, have appointed certain common offi-

cers and have stated in various literature that the two have consolidated their railroad businesses. Petitioners ignore the fact, however, that these acts and practices were the very ones that were contemplated by the ICC when it approved stock control by C&O. See the *Control Case*, 317 I.C.C. at 279, 290-291; *Schleiff* v. *Chesapeake & O. Ry.*, 43 F.R.D. 175, 177-180 (S.D.N.Y. 1967).

2. In their third point (Pet. 30-32), petitioners take issue with the conclusion reached by the Courts below that the "no action" clause of the Indenture constituted a bar to the maintenance of this action. Again they cite no authority to support their position.

Both State Courts and Federal Courts have long recognized that "no action" clauses serve a salutary purpose in prohibiting a multiplicity of suits brought against a corporate obligor by individual bondholders holding only a small number of bonds. See *Schallitz* v. *Starrett Corp.*, 82 N.Y.S. 2d 89, 91 (Sup. Ct. 1948); *Greene* v. *New York United Hotels, Inc.*, 236 App. Div. 647 (1st Dept. 1932), *aff'd mem.*, 261 N.Y. 698 (1933); *Central Hanover Bank & Trust Co.* v. *Siemens & Halske G.*, 15 F. Supp. 927 (S.D. N.Y. 1936), *aff'd per curiam*, 84 F. 2d 993 (2d Cir. 1936), *cert. denied*, 299 U.S. 585 (1936); *Dunham* v. *Omaha & Council Bluffs St. Ry.*, 106 F. 2d 1 (2d Cir. 1939), *cert. denied*, 309 U.S. 661 (1940); *Quirke* v. *St. Louis-S.F. Ry.*, 277 F. 2d 705, 709-710 (8th Cir. 1960), *cert. denied*, 363 U.S. 845 (1960). "No action" clauses prevent bondholders holding only a small number of bonds from instituting suits that may be contrary to the wishes of a large majority of bondholders. Thus, the function of such a clause is not to deny bondholders their day in court but merely to insure that action, if taken, is supported by a substantial number of bondholders. Petitioners also claim that the ownership of some of the bonds by C&O or B&O restricted them in

securing the necessary support of other bondholders in requesting that the Indenture Trustee bring an appropriate action. There is nothing in the record to support this wholly frivolous claim.

3. In the course of their argument petitioners also complain of the fact that the Courts below did not permit them to amend their complaint to allege the proposed three additional alternative causes of action which we have described above (*supra,* pp. 5-6). These additional causes of action sought to be alleged by petitioners are in turn based on two theories, namely, that there was a "merger in fact" of C&O and B&O and that thereby there was an assumption by C&O of the obligations of B&O. Thus, in the first additional cause of action petitioners allege in effect that it must be deemed that C&O assumed B&O's obligations without ICC approval but they do not allege that they acquired their bonds for value in good faith without notice that such alleged assumption was void as required by §20a(11) of the Interstate Commerce Act, an allegation they could not make in view of the fact that they acquired their bonds prior to ICC approval of C&O's stock control of B&O. From what we have already shown, it is obvious that there was no assumption by C&O of B&O's obligations, either *de jure* or in fact, and that there was no reliance by petitioners upon such alleged assumption. For the same reason petitioners' proposed second and third additional causes of action, in which they purportedly rely on §8 of the Interstate Commerce Act (49 U.S.C. §8), are insufficient for petitioners fail to show that either B&O or C&O was under any obligation to apply to the ICC for approval of the alleged assumption by C&O of B&O's obligations and they fail to show any causal connection between the alleged violation of §8 and their claimed damages (see, *supra,* p. 6).

In short, plaintiffs' petition for a writ of certiorari is without any substance or merit.

CONCLUSION

The petition for a writ of certiorari to the United States Court of Appeals for the Second Circuit should be denied.

Respectfully submitted,

EUGENE Z. DUBOSE
Attorney for Respondent
The Baltimore and Ohio
Railroad Company

JOHN L. ROGERS, JR.
RICHARD T. MCDERMOTT
Of Counsel

APPENDIX

APPENDIX A

Pertinent Provisions of the Judicial Code

§ 2321. Procedure generally; process

The procedure in the district courts in actions to enforce, suspend, enjoin, annul or set aside in whole or in part any order of the Interstate Commerce Commission other than for the payment of money or the collection of fines, penalties and forfeitures, shall be as provided in this chapter.

The orders, writs, and process of the district courts may, in the cases specified in this section and in the cases and proceedings under sections 20, 23, and 43 of Title 49, run, be served, and be returnable anywhere in the United States.

§ 2322. United States as party

All actions specified in section 2321 of this title shall be brought by or against the United States.

§ 2323. Duties of Attorney General; intervenors

The Attorney General shall represent the Government in the actions specified in section 2321 of this title and in actions under sections 20, 23, and 43 of Title 49, in the district courts, and in the Supreme Court of the United States upon appeal from the district courts.

The Interstate Commerce Commission and any party or parties in interest to the proceeding before the Commission, in which an order or requirement is made, may appear as parties of their own motion and as of right, and be represented by their counsel, in any action involving the validity of such order or requirement or any part thereof, and the interest of such party.

Appendix A

Communities, associations, corporations, firms, and individuals interested in the controversy or question before the Commission, or in any action commenced under the aforesaid sections may intervene in said action at any time after commencement thereof.

The Attorney General shall not dispose of or discontinue said action or proceeding over the objection of such party or intervenor, who may prosecute, defend, or continue said action or proceeding unaffected by the action or nonaction of the Attorney General therein.

§ 2324. Stay of Commission's order

The pendency of an action to enjoin, set aside, annul, or suspend any order of the Interstate Commerce Commission shall not of itself stay or suspend the operation of the order, but the court may restrain or suspend, in whole or in part, the operation of the order pending the final hearing and determination of the action.

§ 2325. Injunction; three-judge court required

An interlocutory or permanent injunction restraining the enforcement, operation or execution, in whole or in part, of any order of the Interstate Commerce Commission shall not be granted unless the application therefor is heard and determined by a district court of three judges under section 2284 of this title.

§ 2284. Three-judge district court; composition; procedure

In any action or proceeding required by Act of Congress to be heard and determined by a district court of three judges the composition and procedure of the court, except as otherwise provided by law, shall be as follows:

(1) the district judge to whom the application for injunction or other relief is presented shall constitute one member of such court. On the filing of the application, he shall immediately notify the chief judge of the circuit, who shall designate two other judges, at least one of whom shall be a circuit judge. Such judges shall serve as members of the court to hear and determine the action or proceeding.

(2) If the action involves the enforcement, operation or execution of State statutes or State administrative orders, at least five days notice of the hearing shall be given to the governor and attorney general of the State.

§ 1253. Direct appeals from decisions of three-judge courts

Except as otherwise provided by law, any party may appeal to the Supreme Court from an order granting or denying, after notice and hearing, an interlocutory or permanent injunction in any civil action, suit or proceeding required by any Act of Congress to be heard and determined by a district court of three judges.